United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

With affidavit

74-2373

B
B/S

To be argued by
LOUIS BENDER

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

UNITED STATES OF AMERICA,

vs.

ELMER E. HORNBERGER,

Appellant.

On Appeal from Judgment of Conviction, 26 U.S.C. §§7201 and 7206(1); E. D. N. Y., Before Mishler, J. and a Jury

APPELLANT'S BRIEF

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UNITED STATES COURT OF APPEALS
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UNITED STATES OF AMERICA :

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Appellant. :

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APPELLANT'S BRIEF

ISSUES PRESENTED

I. The trial Court erred:

1. In failing to instruct the jury as to appellant's theory of the case, as requested;
2. In striking the Rizzi testimony;
3. In refusing to instruct the jury as requested as to the impact on appellant's intent of the credits to his stockholder's advances and the entries in the books and records, and the trial Court's erroneous charge in these respects was highly prejudicial and reversible error.

II. The trial Court was in error in holding that the burden

of proof was on appellant to show lack of corporate earnings and profits where the Government claimed the omitted income was based on the receipt of constructive dividends. It was thus error to restrict the cross-examination of the Government's expert witness, to refuse to strike his testimony, and to deny judgments of acquittal on all but Counts 9 and 10.

STATEMENT OF PROCEEDINGS

This appeal, pursuant to Title 28, United States Code, Section 1291, seeks review and reversal of the judgment entered on the 13th day of September, 1974 after a conviction by a jury on July 1, 1974, on Counts 1, 2, 3, 4, 6, 7, 9, and 10, in the United States District Court for the Eastern District of New York by the Hon. Jacob Mishler, Chief Judge, which imposed on appellant a term of imprisonment of one year and one day on each count to run concurrently.

These counts on which appellant was charged were as follows: Counts 1 and 2 charged a wilful attempt to evade individual income taxes for 1967 and 1968 in the amounts of $19,334.37 and $66,100.37, respectively, under Section 7201,

Title 26, U.S.C.; Counts 3 and 4 charged appellant with a wilful attempt to evade the income taxes of Story Book Manor, a corporation of which appellant was president, for 1967 and 1968 in the approximate amounts of $2,500.00 and $13,000.00, respectively; Counts 5 and 6 charged appellant with a wilful attempt to evade the income taxes in 1967 and 1968 of Dotal Building Corp., a corporation of which appellant was president, in the approximate amounts of $1,200.00 and $3,400.00; Counts 7 and 8 charged appellant with the wilful attempt to evade the income taxes in 1967 and 1968 of Horn Enterprises, Inc., a corporation of which appellant was president, in the approximate amounts of $3,400.00 and $119.00; and Counts 9 and 10 charged appellant with making and subscribing false U. S. Small Business Corporation returns as president of Story Book Homes, Inc. for 1968 and 1968 in that said returns wilfully understated the taxable income of the corporations for both years in the sums of $11,000.00 and $61,000.00, respectively, in violation of Section 7206(1), Title 26, U.S.C.

Judgments of acquittal were entered with respect to Counts 5 and 8 at the close of the Government's case (732a*, 735a).

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* The letter "a" preceded by a number refers page reference to the Appendix to Appellant's Brief

Motions for judgments of acquittal with respect to the remaining counts were denied (731a) and were likewise denied at the conclusion of the entire case (976a). Oral motions to set aside the verdict on the same grounds previously urged were denied at the time of sentence on the 13th day of July, 1974. Appellant was continued on his own recognizance. A timely notice of appeal was filed on the 23rd day of September, 1974 (1166a).

STATEMENT OF THE CASE

Appellant is 43 years old, married, and has four children (742a-743a). He served in the military of the United States in Korea as an Infantry Sergeant from 1954 to 1956 and was honorably discharged (743a). In 1966 he became a builder of homes and a land developer operating under various corporations (744a). During 1967 and 1968, the years in issue, he operated through several corporations which built homes and developed land primarily in Smithtown, Nesconset, Setauket, and the Townships of Brookhaven and Smithtown (744a). These corporations were Story Book Manor, incorporated October 5, 1961 (GXs 6 and 7, Counts 3 and 4), Dotal Building Corp., incorporated September 17, 1962 (GX 9, Count 6), Horn Enterprises, Inc., incorporated March, 1963 (GX 10, Count 7), and

Story Book Homes, Inc., incorporated February 17, 1960 (GXs 12 and 13, Counts 9 and 10). Appellant was president of all the corporations, sole stockholder, and in complete charge of operations (GXs 6, 7, 9, 10, 12, 13; 744a-745a).

Appellant's functions were: he would attend zoning board meetings, planning board meetings; design homes; work in the field along with his superintendents; buy and sell real estate; develop real estate for other builders; and also build his own homes and assist his salesmen; he would also obtain mortgages from the banks, and keep a rapport with the banks, and he would obtain the mortgages directly (745a). During this period there were employed two full-time salesmen, two part-time salesmen, at least two supervisors, two laborers, an accounts payable girl, and at least two other girls (746a). Of the six girls employed during this period, four testified for the Government, Charlotte Waugh, Vicky Colletti, Constance Haupt, and Rita Perrini (746a). Appellant's accountant was Tom Canale and he and his assistant, Mrs. Paterno, likewise testified (746a). Appellant testified in his own behalf and submitted several character witnesses.

Central to the issue involved was the failure of the

four corporations mentioned to report income in 1967 and 1968 on various "extras" supplied or added to the homes built by these corporations for various purchasers. Such "extras", for example, involved painting, extra land, fuller installation, and various special installations, and the like. This total income involving all corporations amounted to $42,000.00 for 1967 and $113,000.00 for 1968, broken down in the indictment and the proof as follows: six transactions amounting to $11,241.35 charged to Story Book Manor, Inc. in 1967 (Count 3); twenty-two transactions amounting to $37,049.50 to Story Book Manor in 1968 (Count 4); four such transactions amounting to $5,418.34 charged to Dotal Building Corp. in 1967 (Count 5); nine such transactions amounting to $14,221.00 to Dotal Building Corp. in 1968 (Count 6); twelve such transactions amounting to $15,426.00 charged to Horn Enterprises, Inc. in 1967 (Count 7); one such transaction amounting to $1,030.00 charged to Horn Enterprises in 1968 (Count 8); eight such transactions amounting to $10,700.00 charged to Story Book Homes in 1967, charged to appellant under Count 1; and thirty such transactions amounting to $61,226.50 charged to Story Book Homes in 1968, charged to appellant under Count 2.

All of the payments for these "extras" were paid by

check to the appellant personally as distinguished from checks paid to the various corporations involved on the basic price for the house. The "extra" checks were deposited to the individual bank accounts of appellant at the Bank of Smithtown, Eastern National Bank, and Tinker National Bank (GX 142). Appellant, in his opening statement, conceded that the checks for the "extras" were made payable to him rather than to the corporations involved either at appellant's request or at the request of some of his employees; that instructions were issued by appellant to his employees as a matter of company policy to instruct the buyers that the checks for extras were to be paid directly to appellant and not to the corporation involved; and conceded further that the checks for "extras" were deposited in appellant's personal accounts in the Bank of Smithtown, the Eastern National Bank, and the Tinker National Bank (26a-28a).

Appellant entered into a written stipulation which was read to the jury as follows:

> "THE COURT: The parties entered into a written stipulation as follows:
>
> Hereby stipulated and agreed that Government's Exhibits 14 through 107, received in Evidence, represent 92 separate transactions in which buyers paid for extras, that the checks were made payable to the defendant pursuant to his instructions, that the aggregate sum of the extras paid was

approximately $42,000 for 1967 and $113,000 for 1968, dated Brooklyn, New York, June 25, 1974, and signed by Mr. Ryan for the Government and Mr. Bender for the defendant." (361a)

Of the total of $42,000.00 in "extras" deposited in appellant's personal accounts in 1967, $29,475.00 was re-deposited to the various corporate bank accounts in 1967, of which $15,000.00 went to Dotal Building Corp. as against $14,221.91 charged as omitted "extras" in 1968 (Count 6); $19,800.00 to Horn Enterprises as against $15,426.00 charged as omitted in 1967 (Count 7); $3,000.00 to Horn Enterprises as against $1,020.00 charged as omitted in 1968 (Count 8, which count was dismissed); $5,625.00 to Story Book Manor as against $11,241.35 charged as omitted in 1967 (Count 3); $57,760.00 to Story Book Manor as against $37,049.50 charged as omitted in 1968 (Count 4); $3,800.00 to Story Book Homes as against $10,770.00 charged as omitted in 1967 (Count 9); and $62,300.00 to Story Book Homes as against $61,226.50 charged as omitted in 1968 (Count 10). Thus, in 1967 $29,475.00 out of the total of $42,000.00 in omitted "extras" was re-deposited to the corporations in 1968, and $138.060.00 out of a total of $114,659.91 of omitted extras was re-deposited in 1968. Appellant conceded none of the re-deposits of these "extras" from appellant's

personal accounts to the corporate bank accounts was entered in the corporate books as the "extra" corporate income previously paid to the appellant but instead were entered as credits to appellant's stockholder advance account, which appellant claimed was entirely without his knowledge, instruction, or intention.

Appellant conceded at the trial the omission of this income from the corporate returns which he contended was done without his knowledge. His entire defense was that he deliberately directed all home buyers to make "extra" checks payable to him and that he instructed all of his office employees to do likewise in order to forestall any claims against the corporations at the time of title closing of alleged defects in the "extras". Appellant testified that because of difficulty encountered in 1966 with different buyers at the closing of title with respect to disputes over "extras", he believed that if he collected the payments for the "extras" directly he would relieve the corporations of any responsibility for the work done or installation added or additional land purchased in the event there was any claimed defect or other complaint (764a). In that way, appellant believed that the buyers could not delay closing of title with the corporate

seller and the payment of the full basic price to the corporation. It was appellant's further contention that he was holding the "extra" income which he had deposited to his personal accounts for the corporations, that it was his intention to return the moneys to the corporations as soon as it was needed (768a), and that he in fact caused this money to be redeposited to the corporations (768a-769a), with advice to his employee Vicky Colletti that this was money received by him for the "extras" (783a). Appellant further contended that without his knowledge she had treated the funds she received as advances from him (783a) and so noted that fact on checkbook stubs of the corporation in whose bank account the money was deposited, or on the deposit receipt. The accountant Canale had examined some of the entries made by Vicky Colletti, without discussing the matter with appellant, and inferred that these deposits were advances from appellant and accordingly credited the re-deposits to stockholder's advances. Appellant claimed, without contradiction, that he had nothing to do with the books and records (748a), did not know what the entries were, and had left these matters to his employees and his accountant, Canale (786a). His lack of knowledge or direction of the books was confirmed by Canale and his assistant

Paterno, and was undisputed (258a, 272a, 289a-290a). Appellant further testified that he believed Charlotte Waugh, who was in charge of billing the buyers for the "extra" payments and receiving them, had made an adequate record of such receipts in the corporate records (754a, 757a, 759a-760a, 766a, 777a).

In support of appellant's defense to the diversion of the "extra" payments to himself and his lack of knowledge that the re-deposits were credited to his stockholder's advance accounts were the following:

(a) The testimony of Government witness Charlotte Waugh who was in charge of handling the billing and receipt of the "extra" payments to appellant personally, who identified a letter she sent to a buyer early in January, 1967 directing payment of "extras" to the corporation seller (GX 28A-B-C), but that thereafter as a matter of policy all "extras" were directed to be paid to appellant personally (208a, 212a);

(b) The further testimony of Charlotte Waugh that she received all the contracts for 1967 and 1968 (203a) in which the "extras" were listed (205a) and where they were not she probably obtained that information from appellant (207a)

(of the 92 transactions, over 65% of the available contracts reflected that specific "extras" were ordered); that appellant advised her when payments for the "extras" were received by him personally (210a-211a), but that she failed to advise Vicky Colletti that she had been paid the "extras" (213a); that she did not make any entry in any record that the "extras" were paid (214a), believing that the letter that she had sent out on corporate stationery requesting payment for the "extras" was a sufficient record (208a-209a); that she didn't tell appellant she was not advising Vicky Colletti or making receipt of the "extras"; that she knew the "extras" were income and it was her function to see that they were paid (214a-215a) but that she assumed the accountant Canale would have a record of their receipt (215a). She also testified that she kept an index card for each "extra" that was to be paid as a reminder, and when payment was received destroyed the card on her own volition without appellant's knowledge (216a);

(c) She further testified that company policy was to get the buyers to pay for the "extras" before the closing of title (217a) because the mortgagee bank did not want the closing held up in any hassle about the "extras" (217a-218a);

(d) When first interviewed by Special Agent Mazzella on September 14, 1974, appellant advised the Agent that he had

instructed the buyers to make all "extras" payable to him personally and gave the same explanation for doing so mentioned above (522a, 523a-524a, 790a);

(e) Canale and Paterno testified that appellant had nothing to do with the books and records (258a, 328a); they never discussed the entries of the re-deposits to the corporations in the stockholder's advance accounts with appellant (272a, 289a-290a); and that when the tax returns were prepared and presented to appellant, Canale did not discuss the items on the corporate and individual returns but that appellant just signed them (326a-327a);

(f) A total of $248,263.31 was credited to appellant's stockholder's advance account in 1967 and 1968 (320a). Of the $30,000.00 in salary which appellant withdrew in 1967, he returned to the corporation $23,309.00 of his salary in 1967 (321a). Of the $80,000.00 in salary in 1968, he returned to the corporation $55,820.00 in 1968 (321a). A total of $78,144.00 was thus credited to his stockholder's advance account (321a). Appellant drew against his stockholder's advance account for personal reasons in 1967 and 1968 the sum of $56,000.00 (322a-323a), which was less than the total amount of his salary for both years, which had been credited to his

stockholder's advance account. Not one penny of the $156,000.00 representing the "extras" re-deposited but credited to his advance account was touched by appellant; nor was there any proof that appellant used for personal purposes any of the $156,000.00 that had been deposited in his personal bank accounts;

(g) The testimony of the home buyer Rizzi, on direct examination by the prosecutor, that he stopped his check made payable to the corporation for "extras" after appellant had told him to make the check out to appellant personally and that Rizzi did so only after consulting his lawyer who told him that it was all right to do so. This testimony was struck on the Court's own motion in its final charge to the jury.

In contradiction to appellant's testimony, Vicky Colletti said that she did not recall what appellant had told her when he first gave her money to re-deposit to the corporate accounts. She did not know these moneys were for the "extras" paid by the buyers and she assumed the moneys were advances from appellant which she noted on either the checkbook stubs of the corporation in whose bank account the money was deposited or on the bank deposit receipt. The conflict in the testimony between appellant and his employee Vicky

Colletti and the conflict created between the testimony of appellant and the entries of the re-deposits as credits to his stockholder's advances, were crucial issues on which appellant's credibility was paramount. The refusal of the trial Court to properly charge appellant's theory of the defense to the jury, as requested, his striking of the Rizzi testimony, and his erroneous instructions on appellant's responsibility for the entries in his corporate books and records, among other errors during the course of the trial, deprived appellant of a fair trial.

ARGUMENT

POINT I

THE TRIAL COURT ERRED

1. In failing to instruct the jury as to appellant's theory of the case, as requested

Appellant, having conceded, in the opening statement of counsel, in the stipulation before the Court, and in his testimony, that he directed the payments of the "extras" to him for the specific reason that he believed this method of payment would relieve the corporate seller of liability for

any defects and that it was his intention to hold this money for the corporation which he returned in 1967 and 1968, albeit credited to his stockholder's advance account without his knowledge, presented a defense, which if believed by the jury, would have destroyed the requisite criminal intent necessary to convict him on all counts.

Appellant submitted a request to instruct the jury as follows:

> "The defendant claims that he directed the payment of extras be made to him instead of the corporation and thereafter deposited in his personal accounts the extra payments, in the belief this would relieve the corporation of any responsibility in the event the customer sought to make a claim about the extra work done. The defendant further claims that he held these funds belonging to the selling corporation involved with the intention of returning the funds to that corporation, which he asserts he did. It is undisputed that approximately $156,000 representing the total amount of alleged payment of extras to the defendant for both 1967 and 1968 were transferred from the defendant's personal bank accounts to the four corporations involved.
>
> If you accept this contention of the defendant and further find that the entry of these amounts in the corporate books as stockholder advances was made without the defendant's instructions or knowledge, then you must acquit him on all counts because the Government will have failed to prove beyond a reasonable doubt that the defendant had the requisite wilfulness necessary to convict him of attempting to cheat on the corporation's and his own income taxes, as well as to wilfully make

the false statements charged in Counts 9 and 10, even if you were to conclude that the corporations did in fact omit from their tax returns the payments for extras."

The trial Court refused to so charge or even to charge the substance thereof because of his stated but erroneous belief that in doing so the jury might think the Court believed it was so. The colloquy between the trial Court and counsel for appellant is instructive:

"THE COURT: I will not charge the jury on any principle which indicates that if they make findings in accordance with one side's contention or the other, then they must find the defendant guilty or not guilty. ' . . . if you accept this contention of the defendant . . . ' as soon as I see a request like that, it is denied. I will not do that. That again is nothing more than calling the jury's attention to the position of the defendant plus the imprimatur of the Court on it giving it credence. If the jury believes it, it is because of the test and nothing else. Denied.

MR. BENDER: The jury should be told, I think -- would you want me to say anything further about this or shall I stop?

THE COURT: No, go ahead.

MR. BENDER: I think this is the one request which sweeps all the counts. And the jury should be told that if the defendant had this intent, if the jury believes him, that he intended to take the checks for the reasons that he mentioned, and deposit them only to the corporation, and that he in good faith gave them back to the corporation as the corporation's funds, without any knowledge that they were being misentered, then they should

acquit him because then the Government --

THE COURT: I won't say it. I'm going to say if the Government fails to prove criminal intent, to wit, that he knowingly and wilfully filed false and fraudulent returns with intent to evade a substantial portion of the tax, then they must acquit him.

Now, that is saying what you said except eliminates summation by the defendant, because if I say what you want me to say then I should say -- now mind you, if it is not shown -- this is really placing the burden on the defendant which would be wrong, if he doesn't show that he kept this money intending to give it to the corporation, and that he didn't know that the money returned to the corporation was in a column called 'advances' or 'loans' then you must find the defendant guilty. Would you want me to do that?

MR. BENDER: Well, I think to the extent that you are required -- and I say this most respectfully -- in the sense that you are required to charge this jury of the defendant's contention in the case which is set forth in the first paragraph of the request, it may well be that when you give the request then the Government's contrary contention should be given too, but the point is if you don't give the defendant the very contention of his defense in the case it never comes from me with the same force and effect --

THE COURT: I did not say I would not give the position of the parties. That is a little different than summarizing the evidence and pointing to the defendant's position and the evidence supporting it.

MR. BENDER: Well, that is all I thought the first two sentences of the request to charge --

THE COURT: Well, you listen to what I have to say in the charge and you take an exception to it.

> But I will tell you this, nothing that I say is going to indicate that the defendant took this money intending to hold it as corporate funds and that he knew nothing of the books of the corporation. I am not even going to say the defendant contends that is so because that is giving the jury the idea that I believe that that is so." (916a-919a)

In the trial Court's charge on appellant's contentions, the trial Court painstakingly steered away from the substance of this request. Instead, the trial Court directed the jury's attention to appellant's concession that he directed the home buyers to make the checks payable to him and that he deposited them to his own bank accounts, without adding appellant's testimony as to why he did it and whether, if appellant believed in what he was doing, the jury could consider this on the important issue of intent (1089a). Although the trial Court gave appellant an exception to his refusal to charge this request (929a), appellant nevertheless again called this omission to the Court's attention at the conclusion of the charge, but to no avail (1132a). This action of the trial Court, we respectfully submit, was reversible error.

It has been uniformly held that it is reversible error for the trial Court to refuse a request to instruct the jury as to the defendant's theory of the case if there is

evidence in the record to support it. This Court announced its acceptance of this principle in United States v. O'Connor, 237 F.2d 466, 474, n. 8 (1956), where it stated:

> "A criminal defendant is entitled to have instructions presented relating to any theory of defense for which there is any foundation in the evidence, no matter how weak or incredible that evidence may be. United States v. Indian Trailer Corp., 7 Cir., 1955, 226 F.2d 595, 598; Tatum v. United States, 1951, 88 U.S.App.D.C. 386, 190 F.2d 612. 617."

In United States v. Indian Trailer Corp., 266 F.2d 595 (7th Cir. 1955), cited with approval in O'Connor, the defendants were charged with evading corporate income tax by failing to report overceiling payments on trailers the defendant manufactured and sold. The defendant president admitted the receipt of these payments which he kept in a "kitty" pursuant to an agreement with the buyer that he would utilize the overceiling payments for the purchase of scarce materials to manufacture more trailers for them. It was held reversible error to refuse to charge the jury as requested, that the jury should acquit if they found that the defendant president received and kept the money under this arrangement with the buyers, and for this purpose, since if the jury believed the defense contention, there would be an absence of any "wilful

intent to evade taxes." United States v. Indian Trailer Corp., 226 F.2d supra at 598.

The instant case is strikingly similar to Indian Trailer Corp., although the "extras" were kept in the appellant's personal bank accounts rather than, as the defendant did in Indian Trailer, in a separate fund or "kitty", a fact without any real significance, it is submitted.

Also without significance in the instant case is the fact that the evidence of the appellant's theory of diverting the "extras" for the benefit of the corporations came principally from him. Thus, in Tatum v. United States, 190 F.2d 612, 617 (D.C.Cir. 1950), also cited with approval in O'Connor, supra, the Court noted:

> "We do not intend to characterize the case for the defense as either strong or weak. That is unnecessary, for 'in criminal cases the defendant is entitled to have presented instructions relating to a theory of defense for which there is any foundation in the evidence, even though the evidence may be weak, insufficient, inconsistent, or of doubtful credibility. He is entitled to have such instructions even though the sole testimony in support of the defense is his own."

In United States v. Platt, 435 F.2d 789 (2d Cir. 1960), this Court reaffirmed its decision in O'Connor in the respect

previously noted, by reversing a conviction for failing to file income tax returns because the trial Court failed to charge the jury as requested on the defendant's theory of defense of reliance on his accountant. In that case, where the tax returns for 1963 and 1964 were not filed until April 1966, this Court noted that such evidence and other evidence disclosed that "The Government had a strong case" (at 790). Although this Court further noted that the defendant did not take the stand, nevertheless it found some evidence through the testimony of the accountant that the accountant had advised the defendant he had obtained extensions for 1962 and 1963 but had not told the defendant for how long the extensions continued beyond 1963 and 1964. Under these circumstances, said this Court, the defendant was entitled to have the jury instructed that if they believed the defendant understood the accountant to have meant that he had continuing extensions then the defendant should be acquitted since he would lack the requisite wilfulness required. This Court said at 792:

> "We have here the different question whether the record contained an evidentiary basis sufficient to entitle the defendant to an instruction on the defense of reliance. The threshold required for this is not very high:
>
> A criminal defendant is entitled to have instructions presented relating to any

> theory of defense for which there is any foundation in the evidence, no matter how weak or incredible that evidence may be.
>
> United States v. O'Connor, 237 F.2d 466, 474 n. 8 (2 Cir. 1956)." (435 F.2d supra at 792)

Bursten v. United States, 395 F.2d 976, 981-982 (5th Cir. 1968) held the same as Platt that a general instruction on the intent as was done in the instant case was insufficient because the defendant was entitled to a more specific charge in the light of his contention that he relied on the advice of his counsel.

A case also close to the instant situation is Benes v. United States, 276 F.2d 99 (6th Cir. 1960) where the refusal of the trial Court to charge the jury on the defendant's contention contributed substantially to a reversal of his income tax conviction. The corporation of which defendant was the principal stockholder and officer was in the construction business. The defendant built a residence, the Hunting Valley Residence, on property held in the name of his wife for $175,000.00 which was paid for by the corporation and charged on its books to "some seventeen separate customer accounts which the Corporation had on its books at the time of construc-

tion." The office file relating to the construction of the residence was kept by the defendant separate and apart from the other records of the corporation, and his secretary was directed to charge the costs to other projects the corporation had on its books at the time without billing any of these charges to the customers. The items of expense were deducted by the corporation and resulted in a decrease in income taxes, which was the basis of the prosecution. The defendant, some two years after the construction of the residence but after an Internal Revenue agent had questioned appellant about it, filed amended returns to correct what had occurred and issued a promissory note to the corporation for the cost of the house. The Government's theory was that the defendant from the beginning knew that the Hunting Valley Residence was to be his, that he wrongfully diverted the funds of the corporation and realized personal gain as a result. The defendant's theory, however, based primarily upon his testimony, was that his principal purpose at the beginning in building the residence was to provide a corporate project in order to preserve his working force between jobs or to use as a backlog for labor. Said the Sixth Circuit at 104:

> "Still another defect in the charge was the failure of the court to state fully and

> objectively the contentions of the appellant with respect to his purpose in building the residence in Hunting Valley. Appellant testified in substance that the project was first undertaken as a corporate project to preserve his working force between jobs, or to use as a backlog for labor."

and later, at 104:

> "Appellant was entitled to have his theory of the case stated to the jury fully and accurately and without distortion of the essential facts."

In the instant case the prosecutor in his cross-examination of appellant, and in his summation attacked the appellant's purpose in directing that the "extra" payments be made to him personally in a fashion similar to the Government's theory in Benes v. United States. Thus, said the prosecutor,

> "Now, the defendant gives a reason for having all of this $156,000 made payable to himself personally. You're going to have to decide the defendant's credibility. Is he a dumb person: He's a college graduate, majored in Math and Science. He started in this business forming corporations, and by the time of '66 and '67 was doing over a million dollars a year.
>
> Do you really think he was that stupid? . . .
>
> He says that, 'We had some trouble in 1966 with buyers at closings. We were getting into disputes over extras. We were negotiating and I would be reducing the price. At that time checks were made out to the corporations, so I decided to relieve the corporations of this responsibility. That sounds nice, in words,

but when he talks about relieving the corporations of responsibility, remember again, we are not talking about General Motors. We are talking about one man, Elmer E. Hornberger, the president and sole stockholder.

And really what was he relieving them of? If you can believe that. If there is a dispute over extras, delay the closing, demand payment in advance. And if you care to, you can examine the documentary evidence on some of these 93 purchases and you will see, and as Charlotte testified, we wanted money in advance before the construction started.

So really, how does this require checks to be made out to him personally, if there was some problem in disputes over extras and whether or not they were done and done properly? The checks could have been made out to the corporations. . . .

* * * *

So why did the defendant insist that the check be made out to him and not to the corporation? What legitimate reason was there? The reason he gives is to cut down the haggling. What haggling was there from the four buyers we did call? Zero.

How many law suits did he institute in the two years in question? Zero.

So what do you think of the reason of having these checks made payable to him that he offers? You are the judges of the facts. You use your common sense. You put two and two together.

Let me say this: Is there anything wrong if he wants to sue people as an individual, relieve the corporation of this responsibility, to have them make the checks payable to him and just endorse on the back 'Elmer E. Hornberger, pay to

> the order of Story Book Homes' and deposit it into the corporate account? What was to prevent him from doing that, nothing, if he wanted to report this money as income?
>
> What reason was there of depositing it into his personal account as opposed to endorsing the checks over and depositing them into the corporate accounts? What legitimate reason was there? Is there a legitimate reason or is the reason that this man was engaging in an attempt to invade [sic] the taxes on $156,000 payable to him? Can you find a legitimate reason?" (1036a-1041a)

This strong attack on the appellant's position was further proof of the importance of the instruction requested since if appellant's theory was believed by the jury it may have destroyed the prosecutor's contention that the appellant's conduct in failing to report the corporate income on the "extras" was conclusively wilful by the mere fact that he schemed to divert the "extras" to himself and deposit them in his personal bank account.

Appellant's situation was extremely precarious because ordinarily such diversion of corporate funds would in and of itself create an inference of wilfulness (Spies v. United States, 317 U.S. 492, 63 S.Ct. 364 (1943)), but where the tax evasion motive played no part in such conduct, at least as appellant contended, it was error for the trial Court

to refuse to instruct on appellant's evidentiary theory. Levine v. United States, 261 F.2d 747, 748-749 (D.C.Cir. 1958); Koontz v. United States, 227 F.2d 53, 55 (5th Cir. 1960); Strauss v. United States, 376 F.2d 416 (5th Cir. 1967).

Based upon appellant's admissions, the Government's evidence was exceedingly strong, to say the least. Appellant's credibility was seriously attacked and so was his entire defense of lack of wilfulness. Appellant was, at the very least, entitled to have the Court instruct the jury based upon the evidence before it. The reason the trial Court gave for denying it is clearly insufficient as indicated by the authorities cited.

Indeed, the trial Court was patently inconsistent in considering the necessity of instructing the jury on inferences to be drawn from the destruction of corporate records by flood and the appellant's theory of the case, as counsel for appellant sought to point out. On its own volition after summations, the trial Court inquired whether there should be a charge on the destruction of the records (1060a). When counsel for appellant stated, "I would prefer that you didn't make any such charge" (1063a), the Court stated, "I know; but

there is evidence in the record, and you brought a witness in at the end to prove that there was a flood in fact that destroyed the records." (1063a). This was in marked contrast to the trial Court's failure to charge on appellant's theory of the case notwithstanding the existence of evidence before the jury to warrant it.

2. In striking the Rizzi testimony

The trial Court further compounded the error in failing to instruct the jury on appellant's theory of the defense by instructing the jury in its final charge after summations to strike from their minds the testimony of Government witnesses Greshin and Rizzi.

Government witness Greshin, an attorney for one of the buyers, testified that he and his client, Walsh, attended the closing of title at which appellant and his attorney Wolfsont were present. Wolfsont was co-counsel at the time of the instant trial. The witness further testified on direct that he sought to find out why the check for $1,931.00 in "extras" should be paid to appellant personally and not to the corporate seller, Story Book Homes. Greshin said he "was

puzzled over it" (61a) and did not get any satisfactory response from appellant (62a-63a). Nonetheless, at appellant's direction, or at Wolfsont's direction, the check was endorsed over to appellant and delivered to him (63a-64a). The witness admitted on cross that the "extras" for $1,921.00 were included in the closing statement (66a) and that approximately $1,340.00 of that amount was listed in the contract (67a). Greshin further testified on cross that he informed the Internal Revenue Service approximately one year after the closing of title about the payment of the "extras" to appellant personally and sought an informer's reward (69a).

Government witness Richard J. Rizzi testified on direct that he signed a contract with Story Book Homes to build a house in 1967 and that he ordered "extras" from appellant (75a). Rizzi further stated he received a letter from the corporation directing payment of the "extras" (GX 64A) and he made a check payable to the corporation for $1,500.00 (GX 125, 77a). Appellant then called him and "bawled him out" for not following instructions in the letter to make the check payable to appellant personally (78a). Appellant sent the check back (79a). After this conversation with appellant, Rizzi notified his lawyer, he said, and his lawyer ". . . said

it was perfectly all right to make it out to him, so when I received it back I went back and I made up the entire amount for $2,110 to Mr. Hornberger" (GZ 64A; 79a). Rizzi then said he received a letter from the corporation acknowledging receipt of his check made out to appellant for $2,110.00 (GX 64C; 81a), and that all of the "extras" ordered were a part of the contract (82a-83a; Exhibit A).

The Rizzi testimony as to his conversation with his attorney, offered by the Government, unsolicited by appellant, offset in some measure the inferences of wrongdoing created by the testimony of Greshin, the informer attorney. It was significant evidence for appellant to eradicate any such impression of wrongdoing caused by the testimony of Greshin and further to bolster his contention that in deducting payments of "extras" to him he was not, in the opinion of attorney Greshin, knowledgeable in this field, engaging in dubious or wrongful conduct.

Appellant's counsel referred to the Rizzi testimony in this respect as well as in the respect that the "extras" were included in the closing statement and in the contract on summation, and the prosecutor did likewise with respect

to the Greshin testimony. Said the prosecutor:

> "First of all, despite all the documentation under which this defendant was operating no one discovered it. In fact, not even Mr. Greshin discovered it. He suspected." (1048a)

and

> ". . . it was not discovered by the Internal Revenue Service until someone filed a complaint, Mr. Greshin." (1048a)

The trial Court at the very end of his charge to the jury struck the Rizzi testimony as follows:

> "The statement by Mr. Bender that in Mr. Rizzi's lawyer's opinion there was nothing wrong in Mr. Hornberger's request directing Mr. Rizzi to make it payable to him personally, has nothing to do with this case either.
>
> His opinion is totally worthless. He is not here to be cross-examined as to his opinion and just disregard it entirely." (1117a)

In the colloquy between counsel for the appellant and the Court after the charge where counsel took an exception to such action of the Court, the Court intimated that he struck the testimony for the very reason that appellant's counsel sought to use the Rizzi testimony and the Greshin puzzlement as an indication that appellant could not be charged with any criminal intent if the lawyers themselves were in conflict as to the propriety of having "extras" paid to appellant rather

than the corporation (1130a-1151a).

The trial Court was in error in three respects:

(a) Counsel for appellant did not argue to the jury the Rizzi and Greshin testimony as interpreted by the trial court. On the contrary, the jury was told not to construe the Greshin "puzzlement" as indicating anything inherently wrong in appellant's conduct in requesting payment of the "extras" to him but to value Greshin's testimony in the light of Mr. Rizzi's lawyer who saw nothing wrong in Rizzi making out the check for the "extras" to the appellant rather than the corporation, and the further fact that Greshin should not be believed because he was seeking a reward from the Internal Revenue Service (988a-990a).

But even if the trial Court was correct in its interpretation of counsel's argument, the argument was based on evidence in the record; it was proper and relevant on the issue of appellant's intent; and its relevancy and materiality were scarcely a reason for the trial Court to tell the jury to disregard it. The trial Court in doing so undercut appellant's belief that he was not doing anything wrong in directing the "extra" payments to himself.

(b) The Rizzi testimony as to what his lawyer said was not impermissible hearsay which the trial Court implied when in striking the testimony he told the jury that Rizzi's lawyer was not here to be cross-examined. The Government invited the testimony in having the witness explain the reasons why he stopped payment on his $1,500.00 check to the corporation and issued a check made payable to appellant personally for that amount. In striking his testimony for the reasons advanced to the jury, the trial Court was in error. This Court has on several occasions sanctioned the admissibility of such testimony as an "utterance contemporaneous with a non-verbal act . . . relating to that act and throwing some light upon it." United States v. Annunziato, 293 F.2d 373, 377 (2d Cir. 1961); United States v. D'Amato, 493 F.2d 359, 363 (2d Cir. 1974); United States v. Lewis, 447 F.2d 134, 141 (2d Cir. 1971).

(c) In charging the jury that what Rizzi's lawyer said to Rizzi "has nothing to do with this case at all", but that what the jurors shall decide is whether appellant's conduct was engaged in "knowingly and was a wilful attempt to evade his tax" (1117a), the trial Court cut to ribbons, if it did not remove from the jury's consideration entirely, the

importance of appellant's motive in and reason for directing the payment of the "extras" to himself. Had the trial Court instructed the jury as requested, that in determining appellant's intent they should consider his motive for directing the payment of the "extras" to him personally and that he was holding these funds for the corporation as he contended, the error in striking the Rizzi testimony and the trial Court's comments with respect to it would have been less prejudicial; but as it turned out, it resulted "in converting a defense shield, however fragile, into a prosecutor's sword." United States v. Platt, 435 F.2d 789, 793 (2d Cir. 1970).

3. In refusing to instruct the jury as requested as to the impact on appellant's intent of the credits to his stockholder's advances and the entries in the books and records, and the trial Court's erroneous charge in these respects was highly prejudicial and reversible error

The trial Court denied the request contained in appellant's Request No. 1, which in pertinent part provided:

> "If you conclude that the Government has failed to prove beyond a reasonable doubt that the defendant did instruct or advise that the extra moneys returned to the corporations were to be

> credited to him as stockholder's advances, or that the defendant was consciously aware and had knowledge of the fact that the deposits were being credited to his stockholder's advance account as loans from him, then no inference whatever can be drawn against him by the entries in the stockholder's advances in determining whether the extras deposited to the corporations by the defendant were considered by the defendant as belonging to the corporations. See Mertens, Law of Federal Income Taxation, and cases cited, Vol. 2, §§ 10.07, 12.102, p. 401."

With respect to the denial of this part of the request, the trial Court stated:

> "Of course I am going to say nothing about what you say on the third page. I will not carry the ball for you, Mr. Bender. Each lawyer does his own work and the judge won't help either. You go to the jury and argue this." (910a)

Related to this third page of appellant's Request No. 1 was appellant's Request No. 3, which provided:

> "Wherever the issue in a criminal case involves the accused's knowledge of the contents of his books of account in order for the defendant to be chargeable with knowledge of their contents, it must appear that the books and records were kept with his knowledge and under his general direction and supervision."

As to Request No. 3, the trial Court said:

> "I will be most surprised if they [cases cited in Request] are what you say." (913a)

The trial Court reserved decision on it, but gave exceptions

to appellant on these rulings (923a).

These requests, it is submitted, stated the correct law applicable to the determination by the jury of the inferences to be drawn against or in favor of appellant's knowledge of the omission of the extras from the corporate records, the entries in the checkbook stubs of the re-deposits as advances, and the entries of the re-deposits as credits to his stockholder's advances.

Instead, the trial Court charged the jury that they could infer guilty knowledge as to the contents of appellant's corporate records and the credits to his stockholder's advances merely if the jury believed appellant was too busy on construction and other matters to take the time to look at his records. It was contrary to what appellant had requested. The trial Court charged:

> "The defendant has testified that he was an extremely busy man, that he never examined the books of account of his corporations to determine how the payments made by him to the corporations were posted and never discussed the matters as to how extras were treated with his accountant, Mr. Canale; that he never examined the income tax returns that he signed, that might have made him aware that such payments were being treated as advances or loans.
>
> If the Government proves beyond a reasonable

> doubt that the defendant had a conscious purpose in avoiding knowing the contents of the books of account of the corporations, and the matters contained in his income tax returns, in other words, if he refused to examine them and look at them and did that knowingly and consciously, then you may infer from that fact and all the facts and circumstances in the case, if such is the reasonable inference based on common sense and experience, that the defendant knew that the monies deposited from his personal checking account to the corporation accounts were entered on the books of the corporations as advances in loans and as such were not taxable as income either to himself or the corporations." (1108a-1109a)

How was the jury to interpret what the trial Court meant by saying "if he refused to look at them and did that knowingly and consciously" then you can draw guilty inferences "based on common sense and experience"?

Having just instructed the jury that the defendant had testified that he was an extremely busy man, that he never examined the books of account of his corporations to determine how the payments made by him to the corporations were posted, it was more than likely that the jury would interpret this conduct on the part of appellant within the framework of the trial Court's language that appellant refused to look at the records. Obviously, appellant knowingly and consciously did not examine the records, as he testified,

because he was too busy on other corporate matters and he had left these duties to his employees and his accountant.

The charge as given, however, made no exceptions for this evidence given by appellant but permitted the guilty inference even if appellant's refusal to examine his records was due to his other busy duties. On a permissible and reasonable construction of appellant's evidence, appellant's knowing and conscious purpose was not to refrain from examining his records with a tax evasion motive, but because he was busy on other matters and left those chores to his employees and accountant.

In United States v. Pechenik, 236 F.2d 844 (3d Cir. (1956), cited as an authority for appellant's Request No. 3, the Government, as in the instant case, sought to link the defendant with the erroneous corporate books, arguing, as it did in the instant case, that it was incredible that the defendant did not know of the erroneous entries, although the evidence was undisputed that the defendant in that case did not instruct as to the entries or examine the books and records but left them to his employees and accountant, as was the uncontradicted evidence in the instant case. The Third

Circuit noted:

> "Certainly the jury could accept or reject the testimony which exonerated the defendant of evil intent. But disbelief does not supply proof that the defendant participated in, directed or knew the books were kept incorrectly." 236 F.2d at 847.

In Levy v. United States, 92 F.2d 688 (9th Cir. 1937), the Ninth Circuit significantly approved the very charge which appellant had requested in Request No. 3. The Ninth Circuit set forth with approval the charge of the trial Court as follows:

> "Before any entry in such books can be considered by you in determining the guilt of any defendant, it must first be proven to you beyond all reasonable doubt that such defendant made or caused to be made that particular entry, or that it was made with his knowledge and under his supervision. Unless you so find, no entry in the books of account can be considered by you in any manner as proving or tending to prove the guilt of any defendant." (92 F.2d at 691)

The refusal to so charge as requested by appellant of the third page of the portion of Request No. 1 and Request No. 3 and instead the prejudicial charge given deprived appellant of a fair consideration of the evidence by the jury to which he was entitled. This was reversible error.

POINT II

THE TRIAL COURT WAS IN ERROR IN HOLDING THAT THE BURDEN OF PROOF WAS ON APPELLANT TO SHOW LACK OF CORPORATE EARNINGS AND PROFITS WHERE THE GOVERNMENT CLAIMED THE OMITTED INCOME WAS BASED ON THE RECEIPT OF CONSTRUCTIVE DIVIDENDS. IT WAS THUS ERROR TO RESTRICT THE CROSS-EXAMINATION OF THE GOVERNMENT'S EXPERT WITNESS, TO REFUSE TO STRIKE HIS TESTIMONY, AND TO DENY JUDGMENTS OF ACQUITTAL ON ALL BUT COUNTS 9 AND 10

The prosecution advised the trial Court that its claim of omitted taxable income on all counts was based on the constructive dividend theory (9a-10a). This we submit was correct insofar as part of the income charged to appellant in Counts 1 and 2 derived from the omitted "extras" from the corporations other than Story Book Homes referred to in Counts 9 and 10 of the indictment. The latter was a small business corporation where appellant had elected to be taxed as an individual. To that extent the income was not chargeable to appellant as a constructive dividend. Since the income omitted by Story Book Homes was substantial, the jury's verdict might be considered sufficient to prove a substantial tax due and owing by appellant under Counts 1 and 2 unless, as appellant submits, the error committed by the trial Court materially affected the jury's verdict in this aspect as well as previously urged in Point I (1), (2) and (3) as to all counts.

The additional income charged to appellant in Counts 1 and 2 as constructive dividends from the extras omitted from the corporations in Counts 3, 4, 6, and 7 amounted to $77,937.85 excluding the amounts reflected in the acquitted counts, 5 and 8. This amounted to roughly 50% of the total additional corporate income in the sum of $149,541.66 for 1967 and 1968 after subtracting the amounts in Counts 5 and 8. To the extent that appellant was entitled to judgments of acquittal on Counts 3, 4, 6, and 7, the removal from the jury's consideration of these counts and the reduction of the income charged as having been evaded in Counts 1 and 2 is scarcely a diminimis factor in considering the impact of the error alleged.

A basic element of the crime charged under Section 7201 of Title 26 is that a substantial tax is due and owing. Sansone v. United States, 380 U.S. 343 (1965); Spies v. United States, 317 U.S. 492 (1943). In charging that appellant diverted the corporate income on the extras and was chargeable with receipt of constructive dividends thereby, it was the Government's burden to prove that the receipt of such constructive dividends resulted in the omitted income and tax due as charged. Unless the receipt of the constructive dividends constituted income to appellant, the Government would have

failed to prove that the income was received on which a tax was due and owing as alleged.

Taxable income, however, did not exist unless the corporations had sufficient accumulated "earnings and profits" available for distribution of dividends. Sections 301(c)(1), 316, Internal Revenue Code, Tr.Reg. Section 1.316-1(a)(2); Devine v. C.I.R., Slip Sheet Op. No. 130 (2d Cir. 1974), p. 4311; Simon v. C.I.R., 248 F.2d 869, 873 (8th Cir. 1957); Clark v. C.I.R., 266 F.2d 698, 715 (9th Cir. 1959); William H. Kenner, et al., T.C.Mem. 1974-273 (¶ 74,273 P-H Memo. T.C. at 1191). Without such earnings and profits, the receipt of the funds by appellant may have constituted a return of capital invested in which event he would receive no income as charged, or to the extent the amount received exceeded the adjusted basis of the stock he owned may have constituted capital gain in which event the tax due and owing would be substantially lower than the tax charged as due and owing. Section 301(c)(2) and (3), Internal Revenue Code of 1954.

Such "earnings and profits" moreover must be properly reduced by the amount of the proposed tax liability of the corporation for the years 1967 and 1968, including

such additions to the tax as the 50% fraud penalty and interest accrued. Clark v. C.I.R., 266 F.2d 698, 715 (9th Cir. 1959). Most often where criminal tax proceedings are instituted, the tax deficiencies charged in the indictment are substantially lower than the civil figures which generally include non-fraud items as well as items on which fraud may be difficult to prove criminally.

Having said all this, we come to the issue which turns on the propriety of the trial Court's ruling that it was not incumbent upon the Government to prove that these corporations (excluding Story Book Homes in Counts 9 and 10) had sufficient "earnings and profits" in order to establish the existence of taxable income in the form of constructive dividends and substantial tax due and owing as charged in the indictment, but that the burden of proof was on appellant to show a lack of such corporate "earnings and profits". For these reasons the trial Court denied the motions for judgment of acquittal as to Counts 3, 4, 6, and 7, overruled objections to the testimony of the Government expert Revenue Agent Vilardi, admitted over objections the Government's computation of tax due and owing (GX 146), and refused to strike Vilardi's testimony (649a-650a).

The cross-examination of Government witness Vilardi sought to prove that he did not consider the "earnings and profits" of the corporation in computing the additional income and tax charged as a constructive dividend. The trial Court, without fully appreciating the complicated nature of proving income on a constructive dividend theory, brushed aside objections to the prosecutor's questions put to Vilardi as involving "the simple computation that almost every layman can make" (631a), and further addressing the witness Vilardi, ". . . you just used the gradations under the tax law and tax at the rate of the increased income?", and when the witness answered "That's right", the Court added, "I might even be able to do that." (631a)

Before the jury, the Court asked Vilardi to "assume for your purposes that the deposits made during 1967 were the proceeds of the extras performed for the various purchasers that closed title during 1967, do you have an opinion as to what the tax would be?" (635a-636a). Vilardi answered this question, as well as the remaining ones put to him by the prosecutor, by simply taking the total unreported corporate income from the "extras", computing this as additional constructive dividend income to appellant without any affirmative

showing that the corporations had sufficient earnings and profits to construct such dividends (636a-644a). That Vilardi did not even consider the impact of Sections 301 and 316 of the Internal Revenue Code is evident from his admissions to that effect (649a). Appellant accordingly moved to strike his testimony, which was denied (649a-650a).

Actually what Vilardi conceded was that he prepared his schedule of the tax due (GX 146) a month before the trial, simply taking the amounts from the counts in the indictment and reproducing them on his schedule (650a). When appellant sought to cross-examine Vilardi as to the effect of Section 316 on the accuracy of his computations, the trial Court sustained its own objection, saying that Vilardi was not an expert on the tax law but was only an expert on the computations (653a). The trial Court further stated, "I don't know what 316 means. I will have to read it to learn it." (653a). Further cross-examination along these lines was again refused, the trial Court stating, "This witness is not being presented as an expert on tax law. . . . I preclude any further questioning that calls for an opinion on the tax law." (656a).

In the colloquy which ensued between the trial Court

and appellant's counsel, when objection was made to the admission into evidence of Vilardi's computation schedule (GX 146) for failure of the Government to lay a proper foundation based upon the Government's claim of omitted income in the form of constructive dividends (658a), the trial Court refused at first to limit the Government to its charge to unreported income based on the constructive dividend theory (658a-661a), despite the Government's prior assertion that that was its theory at the pre-trial on June 20, 1974 (9a-10a), and appellant's assertion that it was defending on that theory announced by the Government (663a).

Appellant referred the trial Court to this Court's opinion in Dizenzo v. C.I.R., 348 F.2d 122 (1965), which the trial Court at first rejected out of hand because, said the trial Court, "that is not a criminal case" (662a).

The trial Court came around only after appellant's counsel conceded that the constructive dividend theory did not affect Counts 9 and 10 (Story Book Homes, Inc), but that appellant was entitled "to whittle down the tax" and "knock out the counts one by one" (664a), at which point the trial Court said, "Put in that perspective, I could understand. I

thought you were arguing that that defeated the claim." (664a).

In subsequently discussing what the Government was required to prove as to the "earnings and profits" of the corporation, the trial Court questioned whether a "complete audit of every corporation had to be made" (665a), and was advised that such was done here and that revenut agents' reports setting forth proposed civil liabilities against all of the corporations existed (665a). When the trial Court asked of appellant's counsel if the revenue agents' reports revealed surplus earnings sufficient to declare a dividend appellant's counsel answered that "this is the Government's proof. They have to reveal a deficiency beyond a reasonable doubt." (666a).

The trial Court after reading Dizenzo advised the Government "you may be confined to the theory that this was a constructive dividend (670a), and further that "The argument here made is under 316. You cannot have a dividend unless it's declared out of earnings or surplus" (670a).

Although the trial Court was concerned that the Government had failed to prove that the corporations had sufficient "earnings and profits" in 1967 and 1968 to construct dividends, the trial Court interpreted the holding of

this Court in Dizenzo that the burden was on the taxpayer to establish that the corporations did not have sufficient earnings and profits equal to the amounts of extras diverted (673a-675a).

The trial Court further stated that the Government had given the trial Court the revenue agents' reports which reflected the proposed additional civil tax and penalties but that the matter of showing that the proposed taxes reduced the corporations' earnings and profits was a matter of defense (677a-678a).

Appellant argued then (675a), as it does here, that the trial Court was in error because Dizenzo did not lay down a rule of burden of proof applicable to a criminal case where the burden is on the Government to prove one of the essential elements of the offense under Section 7201, Title 26, U.S.C., i.e., a substantial tax due and owing. Dizenzo, appellant submits, dealt with a proposed civil deficiency in income taxes which has uniformly been held to be presumptively correct with the burden on the taxpayer to overcome that presumption. Welch v. Helvering, 290 U.S. 111, 115 (1933). This presumption of correctness is the same whether the proceeding

is in the Tax Court on a redetermination of the proposed tax deficiency asserted or in the District Court. Zeeman v. United States, 395 F.2d 861, 866 (2d Cir. 1968).

In United States v. Lease, 346 F.2d 696, 700 (2d Cir. 1965), this Court put it this way:

> ". . . that a taxpayer challenging the correctness of a tax assessment . . . has the burden of persuading the fact finder by a preponderance of the evidence that the assessment is incorrect . . ."

This Court noted the distinction between that principle of the burden of proof of the Government in a civil case from that in a criminal case when it said:

> "In a criminal case the Government, of course, has the traditional burden of persuasion beyond a reasonable doubt, and a mere assessment cannot there play the same role in proving the Government's case. See Price v. United States, supra, 335 F.2d at 677." United States v. Lease, 346 F.2d supra at 701, n. 12.

In Price v. United States, 335 F.2d 671, 677 (5th Cir. 1964), cited in Lease, the Fifth Circuit likewise noted:

> "Since this is a civil action by the Government to recover a deficiency, the cases involving criminal prosecutions for tax evasion are not apposite because of the greater burden of proof imposed upon the Government in that class of cases."

Dizenzo, it is therefore submitted, merely espouses the general rule that the Commissioner's assertion of additional income based upon the receipt of constructive dividends was presumably correct and it was for the taxpayer to overcome that presumption. Dizenzo reversed and remanded to the Tax Court for further findings because the Tax Court had made none in this respect, and further because the corporation's taxable income for the three years on its face was inadequate to cover in amounts the corporate diversions charged to the taxpayer for those three years. Dizenzo v. C.I.R., 342 F.2d supra at 127, n. 5.

In the instant case the taxable income of the corporations for 1967 and 1968 was likewise inadequate on its face to cover the diversion of the "extras" charged to appellant. Thus, the taxable income reported on the tax returns of Story Book Homes in 1967 was $17,053.07 as against the diverted "extras" of $11,241.35 (Count 3); in 1968 the taxable income on the return was $1,918.73 as against $37,049.50 in diverted "extras" (Count 4); the taxable income reported on the return of Dotal Building Corporation in 1968 was $781.95 as against diversions of $14,221.00 (Count 6); the taxable income reported on the return of Horn Enterprises in

1967 was $2,047.20 as against diversions of $15,427.00 (Count 7).

The Dizenzo holding, moreover, did not involve such fact situations in tax evasions cases where the omitted income charged in the indictment was predicated upon a reconstruction of the income through the bank deposit or net worth methods. In those fact situations unexplained increases in bank deposits over gross reported income or unexplained increases in assets in net worth cases upon properly defined conditions have been held to create a prima facie case which, if not rebutted by the defendant, will satisfy the Government's burden. Holland v. United States, 348 U.S. 121, 75 S.Ct. 127 (1955); United States v. Procario, 356 F.2d 614 (2d Cir. 1966). In such cases, the unexplained excess deposits or increases in assets are deemed prima facie income to the taxpayer because after a thorough investigation eliminating any other non-income sources on their face such an inference has reasonable validity. But this is unlike the instant situation where the moneys charged to be income in the form of constructive dividends may be just as likely a return of capital and thus not income or capital gain in which event the tax due may be as much as 75% less than charged in the indictment for the

years 1967 and 1968.

The trial Court, is is submitted, was thus in error in construing Dizenzo as applicable to the instant case to deny to appellant the relief sought. The trial Court was further in error because his rulings resulted in violating appellant's presumption of innocence which extended to every element of the offense charged. United States v. Berger, 325 F.Supp. 1297, 1303, aff'd. 456 F.2d 1349 (2d Cir. 1972), cert. denied 409 U.S. 892; United States v. Morissette, 342 U.S. 246. The presumption of innocence is the converse of the Government's burden of proof and persuasion beyond a reasonable doubt. United States v. Cummings, 468 F.2d 270, 280 (9th Cir. 1972); cf. Deutch v. United States, 367 U.S. 456, 472 (1961). An essential element of this offense was the existence of a substantial tax due and owing by appellant under Counts 1, 2, 3, 4, 6, and 7. The Government failed to maintain its burden of proof so that the trial Court should have granted judgment of acquittal on Counts 3, 4, 6, and 7 and eliminated from Counts 1 and 2 the additional taxes charged to appellant by virtue of the unproved constructive dividends.

Beyond these errors of the trial Court, the jury was inadequately and improperly instructed on how to determine whether the Government proved a constructive dividend and the correct taxes due and owing on the constructive dividend theory. The same error as above noted permeated the charge. The trial Court failed to advise the jury of Section 316 of the Internal Revenue Code and the regulations issued thereunder as appellant had suggested to the trial Court that it would be required to do (663a), and which it was required to do in defining for the jury what constituted a constructive dividend. Exception was duly taken (1127a).

The fact that the conviction on Counts 9 and 10 may stand unaffected by this claimed error, assuming the Court were to disregard the error urged in Point I (1), (2) and (3), or that the sentence imposed was a concurrent sentence are not factors, it is submitted, which militate against reversal on all counts if the appellant was sufficiently prejudiced by the Court's rulings, or he might have received a lesser sentence than the one imposed. United States v. Barash, 365 F.2d 395, 399 (2d Cir. 1966). As this Court further noted in Barash, it is difficult to determine what "spill-over" effect the error might have had on the jury on the other counts. United States v. Barash, 365 F.2d supra at 403.

CONCLUSION

For the foregoing reasons, the judgment of conviction should be reversed and a judgment of acquittal entered, or a new trial ordered.

Respectfully submitted,

LOUIS BENDER,
Attorney for Appellant

No. 74-2373

UNITED STATES OF AMERICA,

V.

ELMER E. HORNBERGER,
Appellant

APPELLANT'S BRIEF
AND
APPENDIX TO APPELLANT'S BRIEF

AFFIDAVIT
OF MAILING

STATE OF NEW JERSEY, }
COUNTY OF ESSEX, } SS.:

I, RICHARD FRANKS, being duly sworn, deposes and says: that he is over twenty-one years of age; that he served the above captioned matter by depositing 2 true copies on the 4th day of December 1974 of said Appellant's Brief and Appendix, duly enclosed in a postpaid and sealed wrapper, certified mail, return receipt requested, in an official post-office duly maintained and operated by the Government of the United States at Church Street Station, Borough of Manhattan, New York City, and addressed to:

Hon. Robert A. Morse
United States Attorney
Federal Court House
225 Cadman Plaza East
Brooklyn, New York

that being the address within that State designated by him on the previous papers in this action as the place where he then kept an office for the regular transaction of business, between which places there then was and now is regular communication by mail.

Richard Franks

Sworn to before me this 4th
day of December, 1974.

JAY FRANKS
My Commission Expires May 18, 1978
Notary Public of New Jersey